

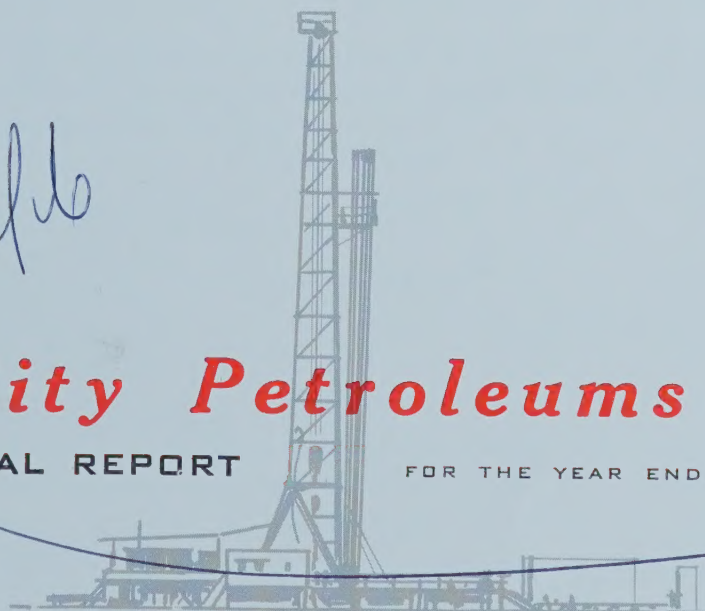
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Mill City Petroleums Limited

ANNUAL REPORT

FOR THE YEAR ENDED DECEMBER 31, 1968



A member of the DYNAMIC GROUP

1968

Fortieth Annual Report

to December 31, 1968

of

MILL CITY PETROLEUMS LIMITED

(Incorporated under the Dominion Companies Act, on August 7, 1929)

AUTHORIZED CAPITAL

6,000,000 shares of no par value

Issued: 5,695,334

REGISTERED OFFICE

210 Fina Building, 736 - 8th Avenue South West
Calgary 2, Alberta, Canada

OFFICERS and DIRECTORS

Roger D. Paugh, President	Calgary, Alberta
Frank Brown, Vice-President	Calgary, Alberta
Robert Clive Brown, Secretary-Treasurer	Calgary, Alberta
Archibald Park Newall, Jr.	Calgary, Alberta
Archibald Park Newall, Sr.	Calgary, Alberta

REGISTRAR

Guaranty Trust Company of Canada Calgary, Alberta

TRANSFER AGENT

Guaranty Trust Company of Canada Calgary, Alberta
Toronto, Ontario

AUDITORS

Peat, Marwick, Mitchell & Co., Chartered Accountants . Calgary, Alberta

BANKERS

Royal Bank of Canada, 8th Avenue and Centre Street . Calgary, Alberta

LISTED

Toronto Stock Exchange

Report of the Directors

TO THE SHAREHOLDERS

The annual report and financial statements of the company for the year ended December 31, 1968 are presented herewith.

CORPORATE AFFAIRS

The company is the beneficial owner of 6,096,694 shares representing 46% of the issued and outstanding share capital of Permo Gas & Oil Limited. In addition the company is the beneficial owner of 425,000 shares of Dynamic Petroleum Products Ltd., 792,000 shares of Royal Canadian Ventures Ltd. and 25,000 shares of Dynalta Oil & Gas Co. Ltd. The quoted market value of the said shares at December 31, 1968, the date of the accompanying balance sheet, was \$15,703,413, whereas at the date of this report the quoted market value of said shares has increased to \$20,384,066. The company's original investment in these shareholdings of associated companies amounted to the sum of \$2,638,662.

FINANCIAL

During the year under review the operations of the company resulted in a net profit of \$135,687 as compared with a net profit during the preceding year of \$206,217. The decrease of \$70,530 is summarized as follows:

	<u>1968</u>	<u>1967</u>	<u>increase (decrease)</u>
Revenue			
Income from production, interest, rentals and royalties	\$333,642	\$298,875	\$ 34,767
Gain on sale of properties	188,008	462,924	(274,916)
	<u>521,650</u>	<u>761,799</u>	<u>(240,149)</u>
Expense			
Exploratory costs, lease rentals, dry hole costs, etc.	101,282	217,910	(116,628)
Administrative and general expense	76,165	152,538	(76,373)
Interest charges	36,984	5,849	31,135
Properties acquired in prior years and abandoned in current year	1,026	8,437	(7,411)
Other	2,728	2,481	247
Depletion and depreciation	167,778	168,367	(589)
	<u>385,963</u>	<u>555,582</u>	<u>(169,619)</u>
Net profit for the year	<u>\$135,687</u>	<u>\$206,217</u>	<u>\$(70,530)</u>

During the current year the company expended the sum of \$182,193 for purposes of exploration and development activity as compared with the sum of \$668,353 expended during the preceding year. The decrease of \$486,160 is summarized as follows:

	<u>1968</u>	<u>1967</u>	<u>increase (decrease)</u>
Acquisition of petroleum, natural gas and mining interests	\$ 1,063	\$390,840	\$(389,777)
Drilling costs:			
Non-productive wells	16,609	109,419	(92,810)
Productive wells	49,976	7,891	42,085
Geological and geophysical surveys	47,180	51,488	(4,308)
Rentals and other carrying charges	37,493	57,003	(19,510)
Production equipment	29,872	51,712	(21,840)
	<u>\$182,193</u>	<u>\$668,353</u>	<u>\$(486,160)</u>

Several large land tracts were farmed out to major and independent companies for considerations involving cash, work commitments and overriding royalties, with a view to increasing the Company's exposure in the industry at minimum cost. As a result the company received \$240,836 in cash during the year and realized a net profit in the sum of \$188,008.

EXPLORATION

GENERAL

The much publicized oil discovery in the Prudhoe Bay area of Alaska has shifted the exploration front and the search for major oil reserves is in new basin areas in the Yukon, Northwest Territories, the Arctic Islands and offshore from both the east and west coasts where the oil and gas industry will expend vast sums in 1969. Your company did not deem it advisable to extend its oil and gas exploration activity into these high cost areas as it was the opinion of the Directors that we had sufficient exposure in the Northwest Territories through our numerous farmout deals involving approximately 1,556,000 acres, together with our direct interest in the Pan Arctic development which includes approximately 4,100,000 acres. Furthermore, the company is represented in the Bristol Bay area of Alaska and in the Inuvik area south of the Arctic coast through its effective control of Permo Gas & Oil Limited and its subsidiary New Continental Oil Company of Canada Limited. As an alternative, the company has stepped up its exploration program in co-operation with associated companies, in the search for base and precious metals and results attained to the date of this report, hereinafter referred to, are indeed encouraging and could materially affect the future prosperity of the company and its shareholders.

SASKATCHEWAN URANIUM OPERATIONS

In 1967 Mill City and associated companies completed an extensive preliminary uranium exploration program covering the entire Athabasca Sandstone area of northern Saskatchewan comprising some 20 million acres. This program involved the flying of approximately 15,000 linear miles of traverses across the subject area using aircraft owned by our group of companies which was equipped with the latest and most modern uranium detection equipment. Results obtained were then interpreted by Seigel Associates Limited of Toronto, consulting geophysicists, and by company geologists.

Following completion of the aforesaid exploration program and the interpretation of the results thereof a joint mineral exploration agreement was entered into with Gulf Minerals Company, a wholly-owned subsidiary of Gulf Oil Corporation, Pittsburgh, U.S.A. Pursuant to the terms of this agreement Gulf conducted an extensive on-the-ground exploration program employing surface geological parties, four diamond drilling crews and support aircraft.

On December 3, 1968 Gulf issued a press release at a press conference attended by the Premier of the Province of Saskatchewan, in Regina, Saskatchewan, to announce that it had drilled an exploratory hole in which it had encountered ore grade uranium mineralization. Such hole was drilled at an angle for a depth of approximately 500 feet and a gamma ray log showed an equivalent average grade of approximately 0.6% uranium oxide (U_3O_8) in selected zones totalling 195 feet. The ore grade indicated is reported to be three times better than that found at Beaverlodge, Saskatchewan, and at least four to five times better than Elliot Lake, Ontario.

Gulf Minerals Company re-entered the Wollaston Lake area in February, 1969 with one drill to commence evaluating and to determine the extent of the 1968 discovery. At the date of this report two more drills have been added to speed the evaluation. Gulf is understandably being very cautious in its approach to announcements concerning its work on the property but they have thus far publicly indicated that three drill holes have encountered high quality ore grade mineralization. On the three permit blocks in the centre of the Athabasca Sandstone basin Gulf has contracted the drilling of a deep test (3,000' to 5,000') which should commence very soon with completion expected in June or July.

Included in this report is a map of the Athabasca Sandstone area including the Wollaston Lake uranium area of the Province of Saskatchewan showing thereon all mineral exploration permits issued according to the best of our information and belief. This map highlights in red the permit lands totalling approximately 1,825,000 acres which are subject to the Gulf agreement and Note 1 thereon indicates the company's direct and approximate indirect interest in the 20% net profits interest retained by the Dynamic Group under the terms of the Gulf agreement. Also shown on this map in red outline is the area of common interest with Gulf encompassing some twenty million acres.

Of particular interest are the three permits comprising some 556,000 acres lying to the southwest of the Gulf-Dynamic Group lands shown on the attached map in light green. These lands are held by the Dynamic Group and Mill City has a 12½% undivided interest therein. Serious negotiations are now under way to complete a joint development agreement on these tracts.

The map included in this report also shows thereon other mineral permits and reservations in the Wollaston Lake uranium area held by companies associated with Mill City, the various retained interests and the extent of the exploration programs to be carried out during the current and subsequent years.

The uranium discovery above mentioned triggered a rush on the part of other individuals and companies, unprecedented in the history of the Province of Saskatchewan, to file on mineral exploration permits in the Athabasca Sandstone area, all of which was covered by the airborne radiometric survey conducted by our group of companies. This discovery could very materially affect the future prosperity of this company and its shareholders.

NORTHWEST TERRITORIES

Mill City is participating with the Dynamic Group in two separate projects in the Northwest Territories. Late last fall staking was completed on an interesting uranium showing and an option agreement has been entered into with a prominent U.S. oil corporation for further exploration of this area during this summer.

In the Baker Lake region, the Group recently acquired a major interest in approximately 375,000 acres of permits. This is a new potential uranium area and will be under active exploration this year by many prominent companies.

BRITISH COLUMBIA

Mill City, in co-operation with associated companies, is continuing its exploration program and the acquisition of mineral claims in the Province of British Columbia through an exploration office established in Kamloops, B.C. Several new groups of mineral claims have been staked or recently acquired and these, together with former holdings, give the company direct interests in many potential mineral areas. Considerable geological and geophysical work has been conducted on many of the claim groups during the past two years with some properties now being scheduled for drilling later this year.

Again, we wish to express our appreciation to all employees and shareholders of the company for their continued interest and loyal support.

Respectfully submitted
on behalf of the Board

ROGER D. PAUGH
President

Calgary, Alberta
May 19, 1969

Mill City Petroleum Limited

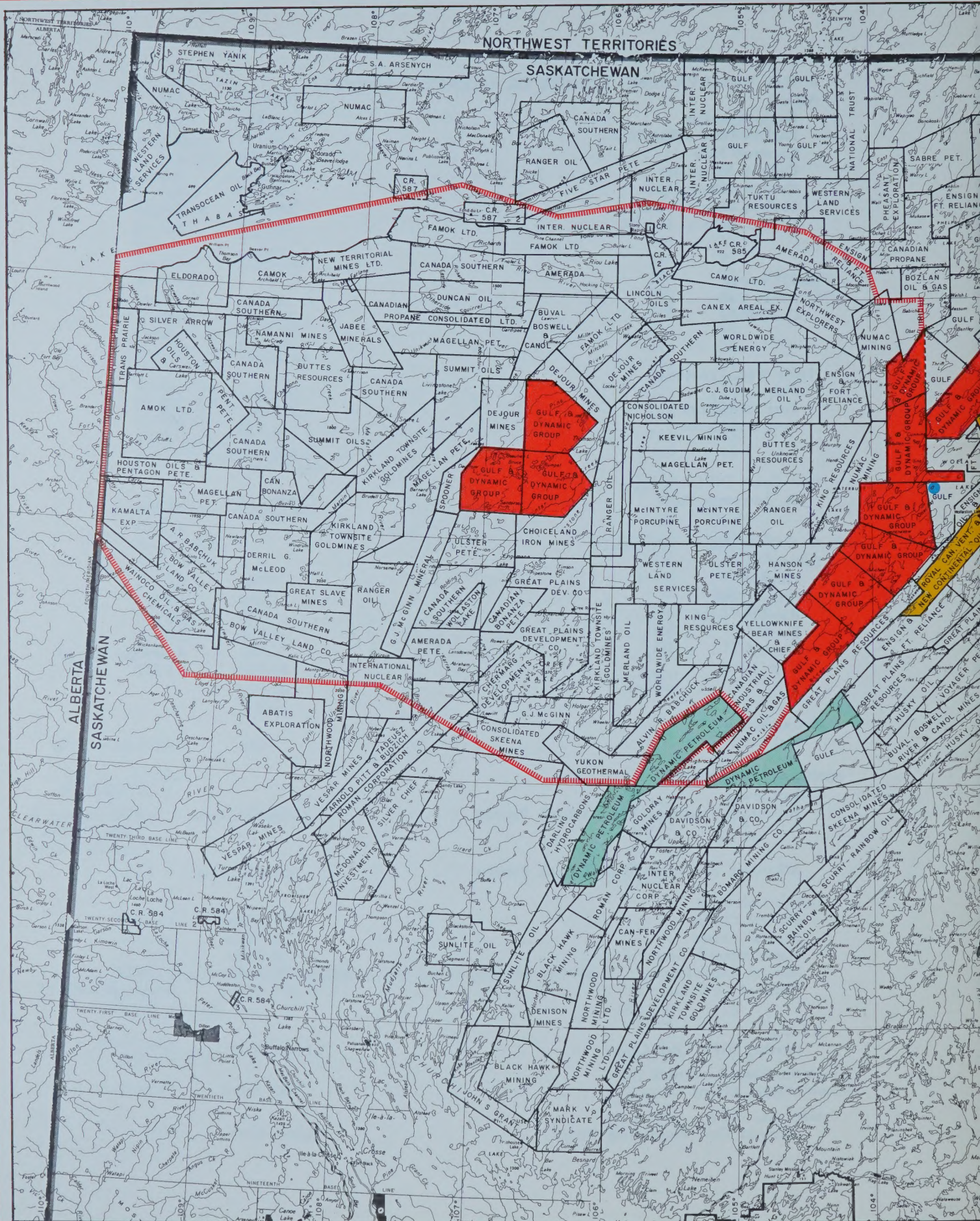
ACREAGE HOLDINGS

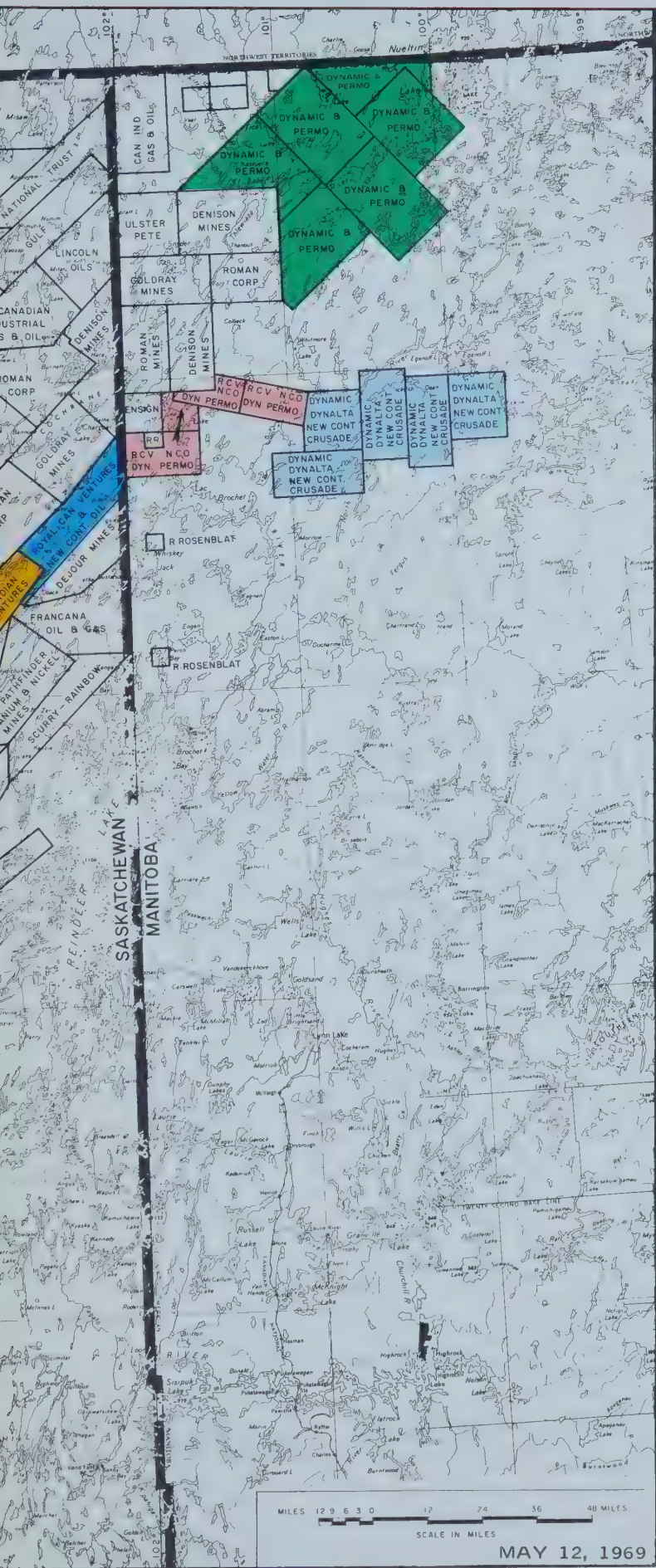
December 31, 1968

PRODUCING P.&N.G. LEASES	ACREAGE	WORKING INTEREST %	
Alberta			
Bonnyville	1,280	100.	
Hussar	3,840	43.125	
Hussar	1,920	14.375	
Hussar	1,760	27.5	
Innisfail	320	1. Net Royalty	
Joffre	80	.9375 GOR	
Leduc	320	100.	
New Norway	160	20.	
New Norway	160	40.	
Pembina	320	1.	GOR
Rainbow	480	25.	
Rainbow	320	12.5	
Turner Valley	40	11.5	GOR
Turner Valley	40	4.	GOR
	<u>11,040</u>		
Saskatchewan			
Hoosier	790	10.	
Midale	79	50.	
Willmar	160	33.3333	
	<u>1,029</u>		
UNITIZED			TRACT FACTOR
Alberta			
Harmatton Elkton Unit No. 1	160	12.5	0.1087
Innisfail Leduc Reef Unit	80	15.	0.1595
Joffre Viking Sand Unit - Seg. A.	440	12.5	2.47568
Kessler Viking Gas Unit (N.G.)	9,760	12.5	11.5884
Kessler Viking Gas Unit (N.G.)	12,960	18.75	
Kessler Viking Gas Unit (P.&N.G.)	2,238	20.	
Kessler Viking Gas Unit (P.&N.G.)	160	25.	
Kessler Viking Gas Unit (P.&N.G.)	160	33.333	0.239963
Turner Valley Unit No. 3	60	100.	
Turner Valley Unit No. 5	40	66.66	
Turner Valley Unit No. 5	40	40.	
Turner Valley Unit No. 7	362	100.	3.92998
Wainwright Unit No. 6	80	50.	7.525313
Wainwright Unit No. 6	20	8.337	
	<u>26,560</u>		

NON-PRODUCING P.&N.G. LEASES	ACREAGE	WORKING INTEREST %
Alberta		
Genesee	640	100.
Haig River	6,080	100.
Jenner	19,634	10.
Joffre	40	12.5
Lochend	320	25.
Lochend	320	25. (Deep-rights)
Lochend	320	12.5 (Deep-rights)
Pembina	1,248	16.6666
Rainbow Lake	320	50.
Rainbow South	320	20.
Steele Lake	640	20.
Stony Plain	320	100.
Turner Valley	4,360	100.
Wainwright	120	50.
Wainwright	160	25.
Wayne-Rosedale	2,480	12.5
	<u>37,322</u>	
Saskatchewan		
Arcola	160	100.
Arcola N.W.	800	33.333
Auburnton	160	33.333
Loomis	3,760	16.666
Loomis	80	25.
Nottingham	560	16.666
Nottingham	160	33.333
Pinto	720	17.5
	<u>6,400</u>	
N. G. LEASES		
Alberta		
Jenner	17,779	10.
Kessler	2,613	12.5
Kessler	7,071	18.75
	<u>27,463</u>	
P. & N.G. RESERVATIONS, PERMITS OR LICENCES		
Alberta		
Margaret Lake	<u>186,240</u>	25
Arctic		
Arctic Islands	100,735	0.6
	3,869,880	5.9044 (Farmout
	<u>160,415</u>	4.2328 Panarctic)
	4,131,030	

P. & N.G. RESERVATIONS, PERMITS OR LICENCES - ROYALTY		INT. %
Alberta	ACREAGE	GOR
Birch Mountain	99,880	0.75
Buffalo Head Hills	30,720	1.5
Cameron Hills	20,480	3.
Caribou Mountains	631,040	2.5
Caribou Mountains	26,880	3.
Caribou Mountains	199,680	1.5235
Legend Lake	139,520	2.5
	<u>1,148,200</u>	
Saskatchewan		
Green Lake	92,160	1.5
Quill Lake	246,517	2.5
	<u>338,677</u>	
North West Territories		
Fish Lake	260,212	2.5
Fort Providence	1,233,942	0.625
Fort Providence	61,920	2.5
	<u>1,556,074</u>	
East Coast Off-Shore		
St. Lawrence Basin	<u>2,320,673</u>	1.6666
P. & N.G. LEASES - ROYALTY		
Alberta		
Chigwell	1,280	2.
Hines Creek	1,280	2.5
Rainbow Lake	320	2.5
Kessler	4,211	2.5
Kessler	640	4. on gas 1.5 oil
High Level	49,920	0.9375
	<u>57,651</u>	
Saskatchewan		
Pinto	640	0.4375 (Deep-rights)
MINERAL INTERESTS		
Saskatchewan		INTEREST %
Athabasca Sandstone Mineral Expl. Permits . . .	1,728,000 acres	12.5% interest in 20% defined net profits interest
Athabasca Sandstone Mineral Expl. Permits . . .	555,800 acres	12.5%
British Columbia		
Mineral Claims	471 claims	14.2857
Mineral Leases	2 leases	14.2857
Placer Mineral Leases	10 leases	37.5
Mineral Expl. Permits - Vancouver Island . . .	126,314 acres	14.2857
Flathead Coal Licences	19,594 acres	Work Requirement + Royalty
Alberta		
Panther River Coal Leases	17,320 acres	50%
North West Territories		
Mineral Claims	200 claims	14.2857
Montana, U.S.A.		
Flathead Coal Prospecting Permit	5,085 acres	90.





WOLLASTON LAKE URANIUM AREA CANADA



GULF 80% AND THE DYNAMIC GROUP 20%

DYNAMIC PETROLEUM PRODUCTS LTD.
ROYAL CANADIAN VENTURES LTD.
MILL CITY PETROLEUMS LIMITED
CONSOLIDATED EAST CREST OIL COMPANY LIMITED
NEW CONTINENTAL OIL COMPANY OF CANADA LIMITED
CRUSADE PETROLEUM CORPORATION LIMITED
DYNALTA OIL & GAS LTD.



AREA OF COMMON INTEREST as defined under the Gulf - Dynamic Group Agreement — approximately 20,000,000 acres.



ROYAL CANADIAN 20%
NEW CONTINENTAL 20%
EXCEL PETROLEUMS LTD. 40%*
SCURRY-RAINBOW OIL LIMITED 20%**

*Subject to an expenditure of \$1,700,000 in a period of four years or less; otherwise the interest reverts to Royal Canadian and New Continental.

**Subject to the proviso that Scurry-Rainbow shall be obligated to assume and pay 60% of such additional expenditures up to a maximum of \$5,000,000.



ROYAL CANADIAN 20%
NEW CONTINENTAL 20%
SCURRY-RAINBOW 40%*
SCURRY-RAINBOW 20%**

*Subject to an expenditure of \$825,000 in a period of four years or less; otherwise the interest reverts to Royal Canadian and New Continental.

**Subject to the proviso that Scurry-Rainbow shall be obligated to assume and pay 60% of such additional expenditures up to a maximum of \$5,000,000.



ROYAL CANADIAN 10%
NEW CONTINENTAL 10%
DYNAMIC PETROLEUM 16%
PERMO GAS & OIL LIMITED 4%
SCURRY-RAINBOW 40%*
SCURRY-RAINBOW 20%**

*Subject to an expenditure of \$678,500 in a period of four years or less; otherwise the interest reverts to Royal Canadian and New Continental.

**Subject to the proviso that Scurry-Rainbow shall be obligated to assume and pay 60% of such additional expenditures up to a maximum of \$5,000,000.



DYNAMIC PETROLEUM 32%
PERMO GAS & OIL LIMITED 8%
SUNLITE OIL COMPANY LTD. 40%*
SCURRY-RAINBOW 20%**

*Subject to an expenditure of \$800,000 in a period of two years or less; otherwise the interest reverts to Dynamic Petroleum and Permo Gas & Oil Limited.

**Subject to the proviso that Scurry-Rainbow shall be obligated to assume and pay 60% of such additional expenditures up to a maximum of \$5,000,000.



DYNAMIC PETROLEUM 25%
DYNALTA OIL & GAS CO. LTD. 25%
NEW CONTINENTAL 25%
CRUSADE PETROLEUM 25%



THE DYNAMIC GROUP 87%



NEW CONTINENTAL 50%
ROYAL CANADIAN 50%

24 Mineral Claims

NOTE 1

The net profits interest retained by the Dynamic Group of Companies under the terms of the Gulf agreement before and after taking into consideration the inter-company share ownership, is shared approximately as follows:

	Direct Interest %	Approximate Indirect Interest in Inter-Company Shareholdings %	Total %
Dynamic Petroleum Products Ltd.	12.50	12.99	25.49
Royal Canadian Ventures Ltd.	12.50	5.00	17.50
Mill City Petroleum Limited	12.50	13.78	26.28
Permo Gas & Oil Limited	—	19.24	19.24
New Continental Oil Company of Canada Limited	12.50	3.57	16.07
Consolidated East Crest Oil Company Limited	12.50	0.26	12.76
Crusade Petroleum Corporation Limited	12.50	0.22	12.72
Dynalta Oil & Gas Co. Ltd.	12.50	0.25	12.75
	87.50	Totals not Applicable	

NOTE 2

Scurry-Rainbow Oil Limited acquired its 20% interest in the various agreements indicated in the legend for a consideration of 15,000 shares of Scurry-Rainbow or \$600,000, and also an undertaking by Scurry-Rainbow to assume and pay 60% of such additional expenditures as may be required up to a maximum of \$5,000,000 on each of the four agreements for a total of \$20,000,000 maximum.

NOTE 3

The permits on this map are in the names of the companies as shown and compiled from information believed to be reliable but not guaranteed.

These permits give the holder the right to explore for all minerals (including uranium) but excepting petroleum and natural gas, coal, and in Saskatchewan, those described as alkali minerals.

Average Permit size - 192,000 acres (300 square miles).

MAY 12, 1969

DECEMBER 31, 1968

ASSETS

	1968	1967
CURRENT		
Cash	\$ 31,357	\$ 5,348
Accounts receivable	136,889	93,055
Government of Canada bonds - at cost (market value 1968 - \$30,875; 1967 - \$16,331)	42,140	21,774
	<u>210,386</u>	<u>120,177</u>
DEPOSITS AND OTHER		
Operating and performance deposits	29,170	58,018
Special refundable tax	1,822	1,822
Agreement for sale	3,653	3,735
	<u>34,645</u>	<u>63,575</u>
INVESTMENTS (Note 2)		
Shares of other companies having a quoted market value, at cost:		
	Market Value	
	1968	1967
Dynamic Petroleum Products Ltd. \$ 1,402,500 \$ 663,000	115,000	115,000
Permo Gas & Oil Ltd. 10,303,413 1,463,207	2,255,777	2,255,777
Royal Canadian Ventures Ltd. 3,960,000 277,200	261,760	261,760
Dynalta Oil & Gas Co. Ltd. 37,500 6,250	6,125	6,125
	<u>\$15,703,413</u>	<u>\$2,409,657</u>
	2,638,662	2,638,662
Shares of and advances to subsidiary companies, at cost less amounts written off	9	2,682
	<u>2,638,671</u>	<u>2,641,344</u>
PROPERTY, PLANT AND EQUIPMENT, at cost (Note 1)		
Producing properties	902,479	1,099,347
Non-producing properties	190,766	301,866
Well development costs	1,127,813	1,296,512
Production equipment	428,109	500,443
Aircraft and other equipment	450,115	208,316
	<u>3,099,282</u>	<u>3,406,484</u>
Less accumulated depletion (\$852,913) and depreciation (\$448,547)	1,301,460	1,749,860
	<u>1,797,822</u>	<u>1,656,624</u>
	<u>\$4,681,524</u>	<u>\$4,481,720</u>

See accompanying

Subject to the accompanying report of Peat, Marwick,

Petroleums Limited

SHEET

with comparative figures for 1967)

LIABILITIES

	<u>1968</u>	<u>1967</u>
CURRENT		
Current portion of bank loans	\$ 150,000	\$ 425,100
Accounts payable and accrued liabilities	107,923	143,706
	<u>257,923</u>	<u>568,806</u>
BANK LOANS (Note 3)	525,000	
Less portion due within one year	150,000	
	<u>375,000</u>	
SHAREHOLDERS' EQUITY		
Capital stock:		
Shares of no par value. Authorized		
6,000,000 shares; issued 5,695,334		
shares	2,072,866	2,072,866
Retained earnings	1,975,735	1,840,048
	<u>4,048,601</u>	<u>3,912,914</u>
CONTINGENT LIABILITY (Note 5)		

Approved on behalf of the Board:

R. C. BROWN, Director

ROGER D. PAUGH, Director

\$4,681,524

\$4,481,720

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tchell & Co., Chartered Accountants, dated March 7, 1969.

Mill City Petroleums Limited

STATEMENT OF INCOME AND RETAINED EARNINGS

For the Year Ended December 31, 1968

(with comparative figures for 1967)

	<u>1968</u>	<u>1967</u>
REVENUE		
Crude oil and natural gas sales less royalties . . .	\$ 442,951	\$ 423,204
Less production and processing costs	120,859	132,315
	<u>322,092</u>	<u>290,889</u>
Royalties	1,326	1,410
Interest	5,306	5,898
Rental	4,918	
Other		678
	<u>333,642</u>	<u>298,875</u>
EXPENSE		
Administrative and general	76,165	152,538
Exploration and survey costs	47,180	51,488
Property carrying costs, lease rentals, etc.	37,493	57,003
Interest	36,984	5,849
	<u>197,822</u>	<u>266,878</u>
CASH EARNINGS FROM OPERATIONS	<u>135,820</u>	<u>31,997</u>
DEDUCT		
Depletion	89,645	101,963
Depreciation	78,133	66,404
Abandonments:		
Petroleum and natural gas and mining interests .	1,026	8,437
Well development costs	16,609	109,419
Loss on sale of securities		2,481
Write-off advances to subsidiary companies	2,728	
	<u>188,141</u>	<u>288,704</u>
ADD		
Gain on sale of properties	188,008	462,924
NET INCOME (Notes 4 and 5)	135,687	206,217
RETAINED EARNINGS, beginning of year	<u>1,840,048</u>	<u>1,633,831</u>
RETAINED EARNINGS, end of year	<u>\$1,975,735</u>	<u>\$1,840,048</u>

See accompanying notes.

Subject to the accompanying report of
Peat, Marwick, Mitchell & Co., Chartered Accountants,
dated March 7, 1969.

Mill City Petroleums Limited

STATEMENT OF SOURCE AND APPLICATION OF FUNDS

For the Year Ended December 31, 1968

(with comparative figures for 1967)

	<u>1968</u>	<u>1967</u>
SOURCE OF FUNDS		
Cash earnings from operations	\$135,820	\$ 31,997
Bank loan, net of amount included in current liabilities	375,000	
Proceeds from shares issued pursuant to stock options granted		16,200
Decrease in operating and performance deposits .	28,848	(18,887)
Proceeds from sale of properties	240,836	491,988
Other	82	460
	<u>780,586</u>	<u>521,758</u>
APPLICATION OF FUNDS		
Purchase of shares of Royal Canadian Ventures Ltd.		101,760
Petroleum and natural gas and mining interests . .	1,063	390,840
Well development costs, including dry holes . . .	66,585	117,310
Production equipment - net	29,872	51,712
Aircraft and other equipment - net	281,919	13,492
Investment in and advances to subsidiaries	55	1,682
Other		2,929
	<u>379,494</u>	<u>679,725</u>
INCREASE (DECREASE) IN WORKING CAPITAL	401,092	(157,967)
WORKING CAPITAL DEFICIENCY, beginning of year .	<u>448,629</u>	<u>290,662</u>
WORKING CAPITAL DEFICIENCY, end of year	<u>\$ 47,537</u>	<u>\$448,629</u>

See accompanying notes.

Subject to the accompanying report of
Peat, Marwick, Mitchell & Co., Chartered Accountants,
dated March 7, 1969.

Mill City Petroleum Limited

NOTES TO FINANCIAL STATEMENTS

December 31, 1968

1. ACCOUNTING POLICY

The Company's Policy is to capitalize the acquisition costs of petroleum and natural gas and mining interests together with drilling and development costs. Carrying costs and exploration expenses are charged against income as incurred. Acquisition costs of producing properties are depleted on a unit of production basis. Well development costs and production equipment are written off over the estimated productive life of the properties. The costs of non-producing properties and unproductive development are charged against income in the year of abandonment.

2. INVESTMENTS

The Company has two foreign subsidiary companies whose accounts have not been consolidated with those of the company because they have been inactive and have no assets. Advances to the companies totalling \$2,728 have been written off in the current year.

Due to the number of shares involved in the investments in other companies, the quoted market value is not necessarily indicative of the amount that could be realized if the shares were to be sold.

3. BANK LOANS

The bank loans are secured by an assignment of interests in certain producing properties and a chattel mortgage on a company aircraft. Although the loans are subject to call on demand, under the agreed terms of repayment, monthly payments of \$12,500 are required.

4. REMUNERATION OF DIRECTORS AND SENIOR OFFICERS

Included in general and administrative expense is an amount of \$38,735, being the Company's share of remuneration paid to directors and senior officers.

5. INCOME TAXES

For income tax purposes, the Company is entitled to claim drilling, exploration and lease acquisition costs and capital cost allowances (depreciation for tax purposes) in amounts which may exceed the related expenses reflected in its accounts. For 1968 the Company intends to claim, for income tax purposes, capital cost allowance in excess of depreciation provided in the accounts. In addition, the company will claim other specified deductions in an amount sufficient to eliminate taxable income.

The Company has filed its income tax returns on the basis that there are sufficient amounts deductible for drilling and exploration expenses to eliminate taxable income for the current and prior years. The Department of National Revenue has questioned the deductibility of certain drilling and exploration expenses applied against income of previous years. The Company does not anticipate that it will have to pay any income taxes in respect of this matter and has calculated that expenditures remain to be carried forward and applied against future taxable income as follows:

Drilling, exploration and lease acquisition costs	\$688,000
Undepreciated capital cost	\$329,600

Management is of the opinion that it is not appropriate to provide for income taxes deferred as a result of timing differences between accounting income and taxable income.

If the Company had followed the deferred tax accounting concept in respect of timing differences for depreciable assets the resulting provision for deferred taxes would have been approximately \$33,000 in 1968. There were no timing differences related to depreciable assets prior to 1968.

If the Company had followed the deferred tax accounting concept in respect of all timing differences between accounting income and taxable income, provisions for deferred taxes estimated at \$39,900 for 1968 and \$84,500 for 1967 would have been required and the cumulative amount at December 31, 1968 would have been approximately \$227,800.

AUDITORS' REPORT

To the Shareholders of
Mill City Petroleums Limited

We have examined the balance sheet of Mill City Petroleums Limited as of December 31, 1968 and the statements of income and retained earnings and source and application of funds for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, except that provision for taxes on income has not been made on the deferred tax basis in respect of depreciable assets as explained in Note 5, these financial statements present fairly the financial position of the company at December 31, 1968 and the results of its operations and the source and application of its funds for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

PEAT, MARWICK, MITCHELL & CO.
Chartered Accountants

Calgary, Alberta
March 7, 1969

